



Before the  
COPYRIGHT ROYALTY BOARD  
LIBRARY OF CONGRESS  
Washington, D.C.

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| _____                                      | ) |                                   |
| <b>In the Matter of</b>                    | ) |                                   |
|  | ) |                                   |
| <b>Mechanical and Digital Phonorecord</b>  | ) | <b>Docket No. 2006-3 CRB DPRA</b> |
| <b>Delivery Rate Adjustment Proceeding</b> | ) |                                   |
|  | ) |                                   |
| _____                                      | ) |                                   |

**TESTIMONY OF EDDY CUE**

1. My name is Eddy Cue and I am global Vice President of iTunes at Apple Computer Inc. (“Apple”). I submit this testimony in connection with and support of the Direct Case of the Digital Music Association (“DiMA”) in the above-captioned proceeding for setting rates and terms for the making and distribution of digital phonorecord deliveries (“DPDs”).

2. I am responsible for the development and marketing of the iTunes Store (which was previously known as the iTunes Music Store) (“iTunes Store” or “ITS”). I was instrumental in the creation and launch of the iTunes Store in the U.S. in 2003. I have worked for Apple for more than seventeen years, and prior to the existence of the iTunes Music Store played a key role in the development of Apple’s Online Store, as well as the engineering and management of Apple’s award-winning iLife suite. I have a bachelors degree in Computer Science and Economics from Duke University.

3. The following testimony is based on my personal knowledge and information made available to me in the course of performing my duties at iTunes.

## I. SUMMARY

4. The iTunes Store offers the public access to an online store catalogue of millions of songs -- each of which has been licensed for distribution from copyright owners -- available for purchase by anyone with a personal computer. As detailed more fully below, purchasing music from the iTunes Store is fast and easy. Consumers need only download the iTunes client application software (the "iTunes Jukebox"), which enables users to interface with the store and also allows them to store, catalog, and playback music downloaded to their personal computers, and to shuttle music to portable devices such as Apple's iPod. After downloading the iTunes Jukebox and clicking on the link to the store, a consumer can browse the store, find music with an easy-to-use and intuitive search engine, listen to 30-second song samples, learn more about new releases, or read reviews from other users about songs or artists of interest to them. Consumers can purchase songs from the iTunes Store with a credit or debit card, using PayPal, or using a prepaid stored-value iTunes Card, and that music purchase is then downloaded directly to the purchaser's personal computer over a fast, secure, and reliable network.

5. In my testimony, I make the following points:

- **iTunes has incurred significant risk and invested tens of millions of dollars launching and growing an online music store aimed at establishing a digital distribution channel for music that is comprehensive, secure, and easy-to-use.** The risks and investments undertaken by iTunes have yielded millions of dollars in revenues for music copyright holders, and filled a much-needed void by providing the public with a lawful, copyright-compliant and customer-friendly means of obtaining music online.

- **The preservation and growth of the online realm as a commercially viable and secure distribution channel for music has required and continues to require substantial ongoing investments, yet the business remains very much subject to erosion from both lawful and, in particular, unlawful competition.** Digital distribution of music is still in its infancy, and its survival as a commercially viable business model is by no means assured. iTunes must constantly replenish its investments in transmission technology, security measures, online site design and capabilities, and customer service simply to compete with well-established brick-and-mortar retail music outlets and to stay ahead of unlawful competition from pirate services that facilitate the unauthorized distribution of music for free.
- **iTunes' retail prices must continue to be positioned as a viable substitute for free music.** The traction in the marketplace gained to date by iTunes is directly attributable to its focus on providing the public with a customer-friendly shopping experience and a price point that represents a viable alternative to the ubiquitous availability of free music from pirate sources. The \$0.99 per track retail price point is key to making the overall consumer value proposition compelling. It maximizes revenues for all industry participants by creating a viable substitute for free music online, thereby encouraging and expanding the lawful consumption of digital music while providing iTunes with a profit margin (albeit a thin one) that encourages Apple to continue to make the investments that are necessary for iTunes' survival and growth.
- **Any increase in the royalty rate for DPDs will reduce aggregate revenues for copyright holders and stall or reverse the growth of lawful digital distribution channels for music.** iTunes' cost structure and margins are not flexible enough to enable the company to incur an increase in the mechanical royalty rate for DPDs without either (i) imposing a retail price hike that will reduce consumption and thereby reduce overall industry revenues or (ii) absorbing the cost input increase, eroding its margin and thereby jeopardizing its continued ability to invest or remain in the business. Based on my experience at iTunes, helping facilitate millions of digital music sales transactions, I have no doubt that an increase in the \$0.99 per track price point would lower total music purchases at the store, stall growth in customer acquisitions, and therefore -- in relatively short order -- reduce overall license revenues paid to copyright holders. Alternatively, if iTunes were forced simply to absorb any increase in mechanical royalty rate, the result would be to significantly increase the likelihood of the store operating at a financial loss -- which is no alternative at all. Apple has repeatedly made clear that it is in this business to make money, and most likely would not continue to operate iTunes if it were no longer possible to do so profitably.



## II. OVERVIEW OF iTUNES

6. When Apple launched the iTunes Store in the United States in April 2003, millions of people already were obtaining music online. However, the overwhelming majority of them obtained that music for free and without the consent of copyright owners by using file-swapping software that facilitated the unlawful trading of music files online. Online distribution of music had certainly proven to be a popular phenomenon, but it was by no means clear whether it could be a successful business that would yield revenues for distributors, record labels, and artists and composers. While the success of Apple's portable music player -- the iPod -- and the popularity of its digital music client software -- the iTunes Jukebox -- had demonstrated the potential commercial appeal of digital music devices, no one had yet succeeded in establishing a viable business model for online sales of digital music. It is never easy to compete against a product that is free, or to persuade people to begin paying for something that they are accustomed to receiving for nothing. The iTunes Store, however, was born out of the belief that people would switch from piracy to the lawful purchase of digital music online -- and that a viable business could be forged online -- if a distributor made it sufficiently easy, convenient, safe, and secure to obtain almost any song they could want at a price point that, while not free, was attractive enough to create an overall value proposition capable of competing with free. A video introduction to our service is attached hereto as Exhibit A.

7. The iTunes music offering consists of the online "iTunes Store," which allows users to purchase permanent downloads of sound recordings, music videos, TV shows, full-length motion pictures, short films, and audio books. Individuals who wish to

access iTunes do so by way of the free iTunes Jukebox client application software, which can be downloaded from the iTunes website. The iTunes Jukebox works on computers running either the Macintosh OSX or Microsoft Windows operating systems and primarily functions as a digital media player. It allows individuals to play back CDs, music encoded or compressed in a wide variety of different formats (including but not limited to the highly popular MP3 format and the Advanced Audio Coding or “AAC” format), and those video files encoded in either the MPEG4 or H.264 formats. When combined with a suitable output device, such as headphones, speakers, or an amplifier system, it turns a user’s computer effectively into a fairly sophisticated stereo.

8. Besides functioning as a digital media player, the iTunes Jukebox acts as a powerful cataloging tool: it allows users to collate and organize their existing personal music collection on their computer. When first downloaded, it finds and sorts any digitally encoded music that might be stored on the computer’s hard drive and collates it into a personal library accessible through the iTunes Jukebox interface. It also allows users to convert music from their personal CDs into digital files for storage on their computer and import that music into their iTunes Jukebox’s so-called “library” in a choice of different digital formats. Once music has been brought into a user’s personal iTunes library, it can either be played back through the computer or be transferred or “synched” to a portable digital media player so that it can be listened to on the move. The iTunes Jukebox is compatible with more than 30 different media players from at least six different manufacturers, including Apple’s own iPod.

9. The iTunes Jukebox also acts as a seamless conduit or interface to iTS. iTS is an online shop, which allows customers to browse through a catalog of over three and a half million songs, as well as thousands of music videos, TV shows, movies, short films and audiobooks, which are available for purchase on an *à la carte* basis for permanent download. Customers can search the catalog by artist, by song and even by genre or era. They can sample music before purchasing by listening to streamed snippets (of no longer than 30 seconds in length) of any of the catalog songs, or they can download the free weekly Single Of The Week (“SOTW”) or Discovery Download, which are provided on the iTS at no cost to the customer for promotional purposes. In addition, customers can look at album artwork and read reviews on the iTS of the songs and albums before they purchase. They can even look at celebrity playlists where a featured celebrity or artist will list his or her top 12 favorite songs that can be purchased at iTS, together with explanations of why each song has significance in their lives. Finally, every time a customer browses or plays songs that are in his or her library of music within the iTunes Jukebox, iTS will suggest or recommend (if the customer chooses to enable the optional “mini-store” function) other songs or albums by the same or different artists that it believes the user may enjoy.

10. Single-track downloads from iTS are sold at \$0.99 per track and full albums are most commonly sold at \$9.99. Customers can pay for purchases with a credit or debit card, using PayPal, or using prepaid iTunes Cards (of varying monetary values). While the majority of iTunes sales consist of consumer purchase of singles for \$0.99, [REDACTED] are sold as part of albums, rather than individually.



11. After browsing, customers with an iTS account can click to purchase their selected songs, which are then downloaded to their computer hard drive and added to their personal iTunes library. Music files purchased through iTS are encoded in the “.m4p” file format, which is essentially the AAC file format combined with the copyright protection provided by Apple’s proprietary “Fairplay” Digital Rights Management (DRM) software. The Fairplay DRM allows iTunes to enforce the content usage rules agreed with the content providers, and to set the parameters within which the songs can be used. For example, once purchased and downloaded from iTS, music can be played back through the computer, copied to a total of up to four other computers, copied or “burned” onto a writeable CD, or transferred, complete with album cover artwork (hardware permitting), onto any portable digital media player compatible with Fairplay technology. At present, songs purchased through iTS can only be directly transferred onto iPods and Motorola phones that are compatible with Fairplay.

12. CDs that are burned using the iTunes Jukebox, and which contain purchased songs, are identical to those purchased from retail outlets such as Wal-Mart, Best Buy or Amazon.com. Just like their counterparts in the physical retail market, they can be played on ordinary CD players. It is even possible to print out album art and song information in the format of a CD Cover to accompany the burned CD using the iTunes Jukebox. And the customer’s ability to quickly and easily access through the store more in-depth information relating to artists, albums, and musical genres of his or her liking can make shopping at iTS a more individualized and rewarding experience than can be found at large physical CD retail outlets, and thereby facilitates repeat visits and additional music purchases.

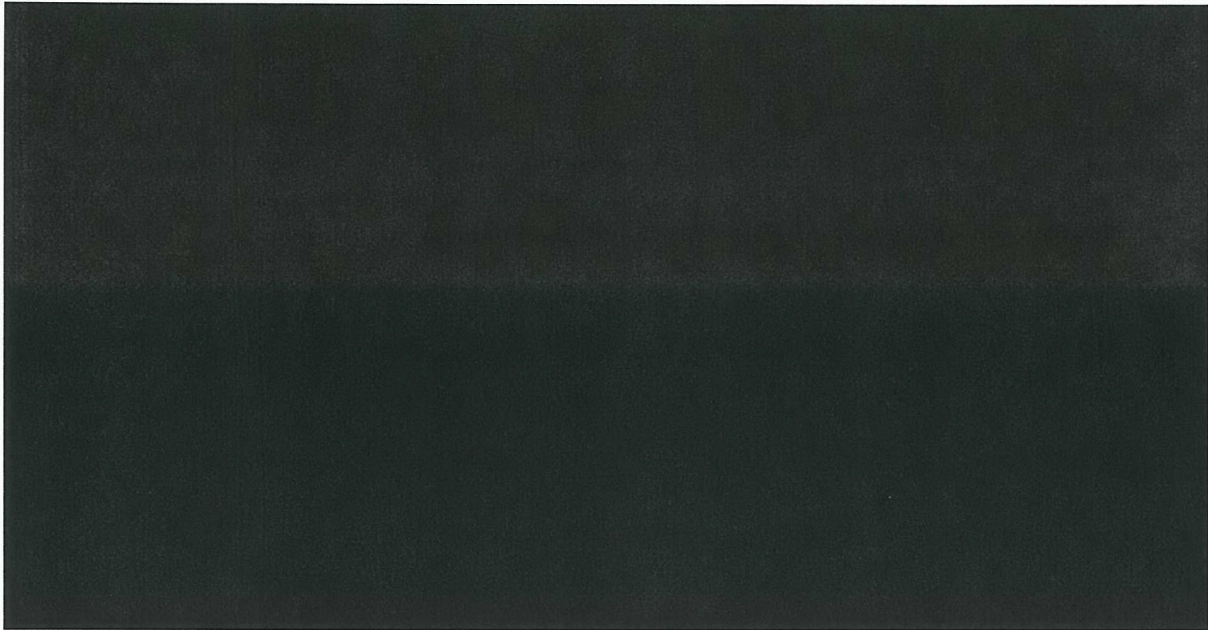


**III. iTUNES PROVIDES A COMPELLING AND VALUABLE OFFERING THAT BENEFITS BOTH COPYRIGHT OWNERS AND CONSUMERS**

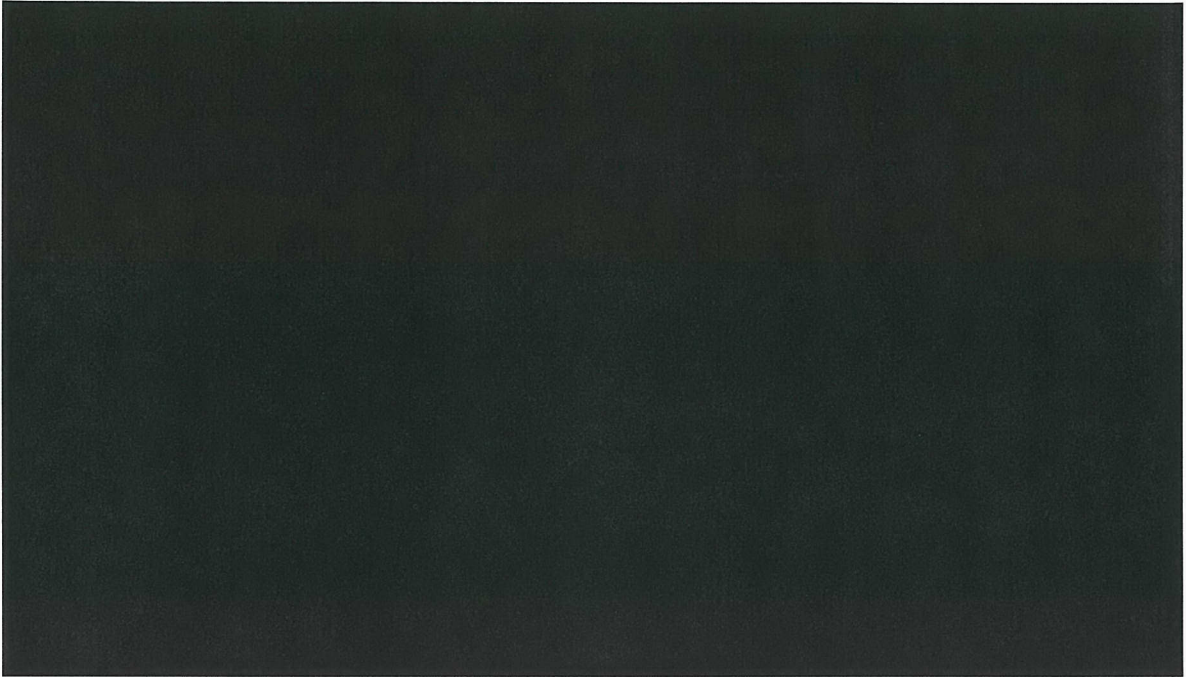
**A. iTUNES HELPED CREATE AND CONTINUES TO GROW A LEGITIMATE ONLINE MUSIC MARKETPLACE.**

13. When the iTunes Store opened to the public in April 2003, there were millions of Americans already accustomed to obtaining music on the Internet -- mostly for free and mostly without authorization from copyright holders. The iTunes Jukebox and iTS provide the public with a lawful and user-friendly means to research, organize, sample, store, and purchase music digitally. The Justice Department's Antitrust chief recently stated that the service has seemed to solve "a problem that some observers, less than five years ago, predicted might never be solved: how to create a consumer-friendly, yet legal and profitable, system for downloading music and other entertainment from the Internet." It took iTS nearly a year before it reached its one millionth customer. Since the beginning of 2005, iTunes [REDACTED] [REDACTED] (with significantly higher growth around the holidays, in part due to our successful marketing of iTunes gift cards).

**Table 1**



14. At the time of iTS' launch, copyright owners viewed digital distribution as an insecure platform for music. Today, we feature a catalog consisting of over 3.5 million songs, all licensed from copyright holders for distribution via iTS.

**Table 2**

A comprehensive schedule of songs and accounts added is attached at Exhibit B.

**B. iTUNES PROVIDES A COMPELLING CONSUMER EXPERIENCE THAT INTRODUCES CUSTOMERS TO NEW MUSIC.**

15. The growth of iTS is the product of digital functionality and capabilities designed to provide customers with a reliable and user-friendly retail experience that helps them navigate an enormous music catalog to find and purchase whatever music they are seeking, and increases their exposure to other (in many cases previously unknown) music that they might like -- all with a view toward expanding sales and demand. The painstakingly designed storefront that greets customers who visit the iTS is critical to the success of the store. As an example, the graphic below show the appearance of the iTS Music home page.





16. The store's interface is designed to make it as easy as possible for people to search, browse, sample, and purchase music. Customers are greeted with a variety of featured content, lists showing (and links to) featured tracks and songs and albums that are most popular on iTS at the time, and easy links to the many music exploration sections of the store. Among many other features, customers can search the store for songs or artists they are interested in using our advanced content search engine; listen to a 30-second preview of any of the more than 3.5 million songs available from the store; download one or more free singles every week, specially selected by iTunes editorial staff each week; learn about new releases and songs generating buzz through the New Music Tuesday email or interactive podcast or by clicking on any of the albums featured in the "swooshes" (interactive banners) and "bricks" (brick-shaped banners) found on the



store's home or genre home pages; read album reviews and artist biographies for music and artists of their choice; browse the iTunes Essentials collections of recommended song collections (by artist, genre, or other topic, such as holiday music) created by iTunes editorial staff; and check out the iTunes Originals live performances (and interviews) recorded exclusively for iTunes. The graphics below show examples of an artist biography page and an iTunes Essentials collection created by our editorial staff.

The screenshot shows the iTunes artist biography page for Beyoncé. The page has a light blue background and a navigation bar at the top with links: Home, Music, R&B/Soul, Beyoncé, and Biography. A "Sign In" button is in the top right corner. The main content area is divided into two columns. The left column contains the artist's name "Beyoncé" in a large font, followed by her birth name "Beyoncé Giselle Knowles", her birth date "September 04, 1981 in Houston, TX", her genres "R&B/Soul, Dance, Contemporary R&B, East Coast Rap", and her years active "'90s, '00s". A small photo of Beyoncé is shown next to this information. Below this is a section titled "Biography" with three paragraphs of text. The right column contains three buttons: "SEE ALL BEYONCÉ", "ALERT ME", and "TELL A FRIEND". Below these are two sections: "FOLLOWERS" with the name "Natalie" and "CONTEMPORARIES" with a list of artists: Kelly Rowland, Justin Timberlake, Ashanti, Craig David, TLC, Michelle Williams, Ciara, Christina Aguilera, Janet Jackson, and Monica.

**Beyoncé**

BIRTH NAME: Beyoncé Giselle Knowles

BORN: September 04, 1981 in Houston, TX

GENRES: R&B/Soul, Dance, Contemporary R&B, East Coast Rap

YEARS ACTIVE: '90s, '00s

**Biography**

Beyoncé Knowles is one of the many impressive artists of the new millennium, but an individual in her own right. She's praised for her wildly inventive presentations in music and film, and respected for her down-to-earth persona. With her grace, beauty, charm, and gift for entertaining, Knowles has become a star and an American icon.

Born in Houston in the fall of 1981, Beyoncé Giselle Knowles started performing at age seven. From dance classes to singing in the church choir, Knowles was a natural. She and cousin Kelly Rowland met Latavia Roberson during this time, and the trio formed a group with Letoya Luckett. Mathew Knowles, Beyoncé's father and Rowland's legal guardian, signed on to be the girls' manager. This situation would ultimately lead to the formation of one of the greatest female R&B groups of all time — **Destiny's Child**.

**Destiny's Child** made its debut 1990 and within ten years, the vocal act had experienced personal and political highs and lows that fueled the group's desire to make it big. **Destiny's Child** sold 33 million albums worldwide by 2002 and earned a slew of Grammys and additional music awards. "Jumpin' Jumpin'," "Bills, Bills, Bills," "Say My Name," and "Survivor" were smash hits, and the group appeared unstoppable.

In 2001, Knowles, Rowland, and Michelle Williams allowed themselves a break from the singing group and tried their hands at individual solo careers. Before landing several movie roles,

**SEE ALL BEYONCÉ**

**ALERT ME**

**TELL A FRIEND**

**FOLLOWERS**

Natalie

**CONTEMPORARIES**

Kelly Rowland  
Justin Timberlake  
Ashanti  
Craig David  
TLC  
Michelle Williams  
Ciara  
Christina Aguilera  
Janet Jackson  
Monica

**'90s Alt Rock**  
Various Artists  
Release Date: Mar 08, 2005  
Total: 25 songs  
\$24.75 [BUY ALL SONGS](#)

**The Basics**  
It started in the Pacific Northwest and emerged as the last great rock upheaval... before becoming a catchall term for nearly every style of music that included guitars. From grunge to rap-rock, these are the alternative-rock radio staples that followed 'the year punk broke.'

[TELL A FRIEND](#)

| Name                      | Time | Artist         | Album                  | Price                           |
|---------------------------|------|----------------|------------------------|---------------------------------|
| 1 Smells Like Teen Spirit | 5:01 | Nirvana        | Nevermind              | \$0.99 <a href="#">BUY SONG</a> |
| 2 Jeremy                  | 5:19 | Pearl Jam      | Ten                    | \$0.99 <a href="#">BUY SONG</a> |
| 3 Loser                   | 3:56 | Beck           | Mellow Gold            | \$0.99 <a href="#">BUY SONG</a> |
| 4 Creep                   | 5:33 | Stone Tem...   | Core                   | \$0.99 <a href="#">BUY SONG</a> |
| 5 Sabotage                | 2:58 | Beastie Boys   | Ill Communication      | \$0.99 <a href="#">BUY SONG</a> |
| 6 You Oughta Know         | 4:09 | Alanis Mori... | Jagged Little Pill     | \$0.99 <a href="#">BUY SONG</a> |
| 7 Basket Case             | 3:03 | Green Day      | Dookie                 | \$0.99 <a href="#">BUY SONG</a> |
| 8 Losing My Religion      | 4:29 | R.E.M.         | Out of Time            | \$0.99 <a href="#">BUY SONG</a> |
| 9 Closer                  | 6:13 | Nine Inch ...  | The Downward Sp...     | \$0.99 <a href="#">BUY SONG</a> |
| 10 Wonderwall             | 4:18 | Oasis          | (What's the Story) ... | \$0.99 <a href="#">BUY SONG</a> |
| 11 What I Got             | 2:51 | Sublime        | Sublime                | \$0.99 <a href="#">BUY SONG</a> |
| 12 Come Out and Play      | 3:17 | The Offspri... | Smash                  | \$0.99 <a href="#">BUY SONG</a> |
| 13 Been Caught Stealing   | 3:34 | Jane's Addi... | Ritual de lo Habitual  | \$0.99 <a href="#">BUY SONG</a> |
| 14 Mysterious Ways        | 4:03 | U2             | Achtung Baby           | \$0.99 <a href="#">BUY SONG</a> |
| 15 Black Hole Sun         | 5:18 | Soundgarden    | Superunknown           | \$0.99 <a href="#">BUY SONG</a> |
| 16 Buddy Holly            | 2:39 | Weezer         | Weezer                 | \$0.99 <a href="#">BUY SONG</a> |
| 17 Just a Girl            | 3:29 | No Doubt       | Tragic Kingdom         | \$0.99 <a href="#">BUY SONG</a> |
| 18 All Apologies (Live)   | 4:23 | Nirvana        | MTV Unplugged i...     | \$0.99 <a href="#">BUY SONG</a> |
| 19 Killing in the Name    | 5:14 | Rage Again...  | Rage Against the ...   | \$0.99 <a href="#">BUY SONG</a> |
| 20 Would?                 | 3:28 | Alice In Ch... | Alice In Chains: G...  | \$0.99 <a href="#">BUY SONG</a> |
| 21 The Beautiful People   | 3:38 | Marilyn Ma...  | Antichrist Superstar   | \$0.99 <a href="#">BUY SONG</a> |
| 22 Miss World             | 2:59 | Hole           | Live Through This      | \$0.99 <a href="#">BUY SONG</a> |

17. iTunes also provides recommendations for other songs and artists in which a customer might be interested. Each time a customer views a particular album within iTunes, iTunes gives the customer information about music that other customers interested in the same music also bought on iTunes (as shown in the graphic below).



The screenshot shows the iTunes interface for the album 'Eyes Open' by Snow Patrol. The top navigation bar includes 'Music', 'Alternative', 'Snow Patrol', and 'Eyes Open'. The album cover is displayed on the left, with the title 'Eyes Open' and genre 'Alternative' below it. The release date is 'May 09, 2006', and it contains '12 songs, 1 booklet'. The price is '\$9.99' with a 'BUY ALBUM' button. A 'Gift This Music' link is also present. To the right, there are links for 'SEE ALL ALBUMS', 'ALERT ME', and 'TELL A FRIEND'. Below these are sections for 'TOP SONGS' and 'LISTENERS ALSO BOUGHT'. The 'TOP SONGS' section lists 'Chasing Cars', 'Run', 'Chocolate', 'Hands Open', and 'Open Your Eyes'. The 'LISTENERS ALSO BOUGHT' section lists 'Continuum' by John Mayer, 'The Last Kiss (Original Motion Picture Soundtr...' by Various Artists, 'Dusk and Summer' by Dashboard Confessional, 'Under the Iron Sea' by Keane, and 'Stadium Arcadium' by Red Hot Chili Peppers. At the bottom, a table lists the tracks from the album.

| Name                            | Time | Artist      | Album     | Price           |
|---------------------------------|------|-------------|-----------|-----------------|
| 1 You're All I Have             | 4:32 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 2 Hands Open                    | 3:15 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 3 Chasing Cars                  | 4:25 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 4 Shut Your Eyes                | 3:15 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 5 It's Beginning to Get to Me   | 4:33 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 6 You Could Be Happy            | 3:02 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 7 Make This Go On Forever       | 5:45 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 8 Set the Fire to the Third Bar | 3:22 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |
| 9 Headlights On Dark Roads      | 3:29 | Snow Patrol | Eyes Open | \$0.99 BUY SONG |

In addition, if a customer has chosen to use the optional Mini Store functionality of the iTunes Jukebox, when the customer selects a particular track in his or her iTunes Library, the iTS Mini Store – which (as shown in the following graphic) appears directly below the Library display – will provide the customer with information regarding content by the same and other similar artists that is available for sale in iTS. The customer then can enter the full iTS directly from the Mini Store, and preview and purchase any of the music recommended by the Mini Store.



18. Customers also can encourage others to explore music available on iTunes through our “Tell A Friend” email functionality (which allows a customer to send friends an email with a link to a particular album available on iTunes), by creating and publishing to iTunes, for all customers to see, an iMix collection of tracks selected by the customer (which the customer also can email to friends with a link to iTunes), and even by gifting particular tracks or albums to friends via email.

19. By providing the public with a single source for millions of musical compositions, background information about the songs and the artists, short samples of every song available for purchase, and cross-references to other recordings and artists reflective of a user’s interests and tastes, iTunes functions not only as a retail outlet for music purchases but also as an informational and promotional vehicle for hundreds of



thousands of artists, many of whose works are not readily available at physical retail outlets. iTunes provides anyone who downloads the free iTunes Jukebox software a powerful music exploration tool, and many people clearly use the store as an easy to access and comfortable information resource and sampling mechanism, as evidenced by the fact that in customers on average stream-sample about nine songs before purchasing one.

20. Thus, even though some customer traffic may not yield an immediate purchase from iTunes, the added exposure to new songs and new artists unquestionably has a multiplier effect -- translating into sales on other occasions and at other outlets, just as in the physical world. Recently, *BillBoard* (September 2, 2006) reported that James Blunt's "Back to Bedlam" is the third-highest-selling artist of 2006 with 2.1 million units sold in the United States and more than 10 million copies worldwide since 2004:

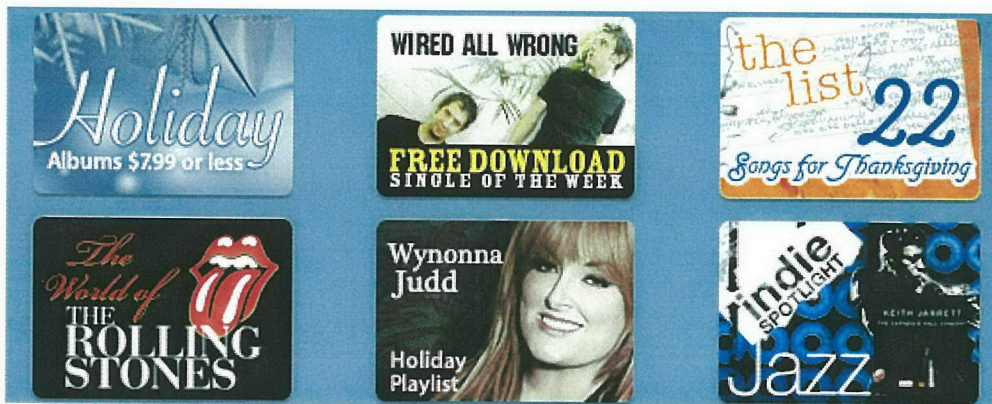
Atlantic released it in Blunt's native United Kingdom a full year before his October 2005 debut stateside. In North America, the company used an Internet campaign that started with months of seeding music and info on tastemaker blogs, bulletin boards and music-community Web sites to build an audience for the album. Blunt also received early championing from digital services including AOL Music, Yahoo, MySpace and iTunes.

This multiplier effect, in which an artist or song's early success on digital services like iTunes contributes to considerable success later in terms of physical CD sales has repeated itself on numerous occasions. For example, only a short time ago Death Cab for Cutie was an independent label band with an intensely loyal, but not widespread, fan base. Death Cab for Cutie's music was featured prominently on iTunes, and the band did a special recording session for the store, the "Studio X Sessions," that went to number one on iTunes. This was followed by an iTunes Originals release that featured more new

Death Cab for Cutie songs -- all of which stoked interest in the band from major labels and helped propel their major-label debut release for Atlantic (a part of the Warner Music Group), “Plans,” to sales exceeding 700,000 units in the U.S.

21. Other bands such as Fall Out Boy, Panic! At the Disco, and Cute is What We Aim For all were able to parlay initial success on iTunes into a greatly expanded fan base and significant overall sales throughout the U.S. Meanwhile, artists such as Joshua Radin, Kate Havnevik, and Sandi Thom each obtained recording deals from major labels after their music gained prominent exposure on iTunes. iTunes’ “developing artist program” continues to nurture talented new artists that have yet to gain significant radio or retail store exposure, raising the profile of bands like She Wants Revenge and Under the Influence of Giants.

22. One unique element of the iTunes storefront is that *none of the songs or artists* that are featured in the store, including on its home page, on a given day are there as a result of any consideration from the artists or their labels. The graphics below show examples of how we use iTunes’ “swooshes” (which can be navigated with the arrows on each side to reveal additional featured content) and “bricks” to highlight content available for sale on the store.



As always, all of the above content was selected by iTunes editorial staff in its sole discretion, in this case to be featured on the iTS Music home page. We pride ourselves on our unfettered editorial discretion, which allows us to focus our features on music we believe customers will enjoy, and allows us to build a relationship of trust and confidence with our customers. From the beginning, iTS has been “all about the music.” Those artists and songs that are highlighted in the storefront are selected mainly to expose our customers to a broad swath of music and drive interest in, and purchases of, musical works that might not otherwise come to the attention of our customers. While the artists and their labels certainly work with us when one of their songs is selected by iTunes to be

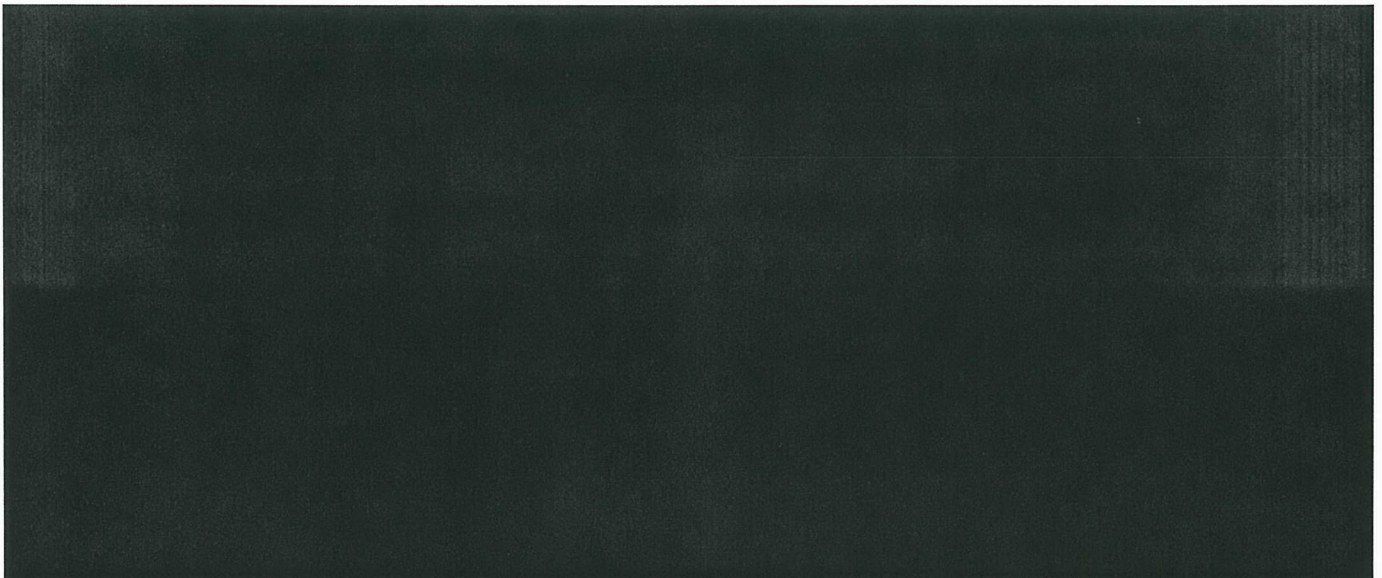


featured in a “swoosh” or “brick,” or chosen by iTunes as a Single Of The Week, there is no advertising on iTS, no sponsored banners from record labels, and no payment for any placement on the storefront. This “music first” emphasis has helped to strengthen our customer relationships, engendering loyalty and earning iTunes plaudits from independent labels, which typically cannot afford the high marketing and promotional incentives associated with obtaining prominent exposure at physical retail outlets.

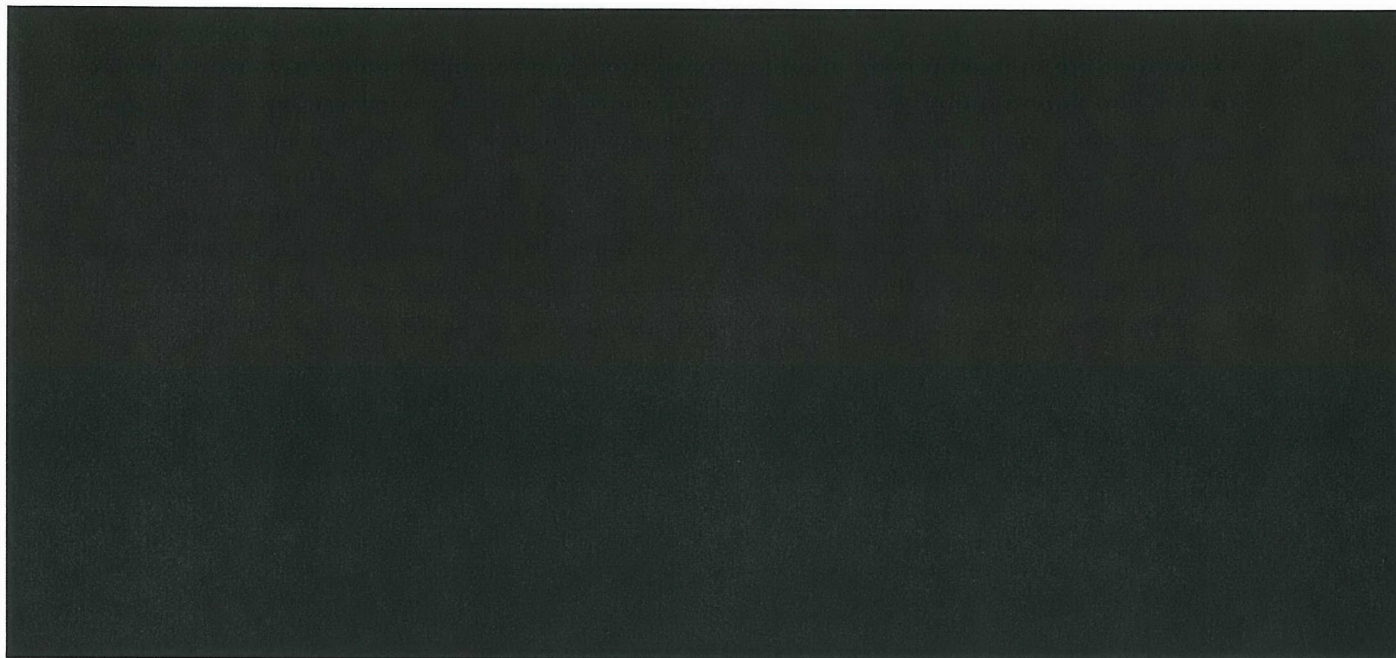
23. A key promotional feature of iTS is the “Single Of The Week,” which (along with another similar program, the “Discovery Download”) each week offers customers a free download of a song from an up-and-coming band or artist. When we select a particular song as the SOTW, we will obtain from the record label in question an authorization to offer it to the public at no charge on a royalty-free basis during the one week period in which it is featured as the “Single of the Week.”

24. As set forth below, the SOTW has had a significant impact on driving sales of music from new artists:

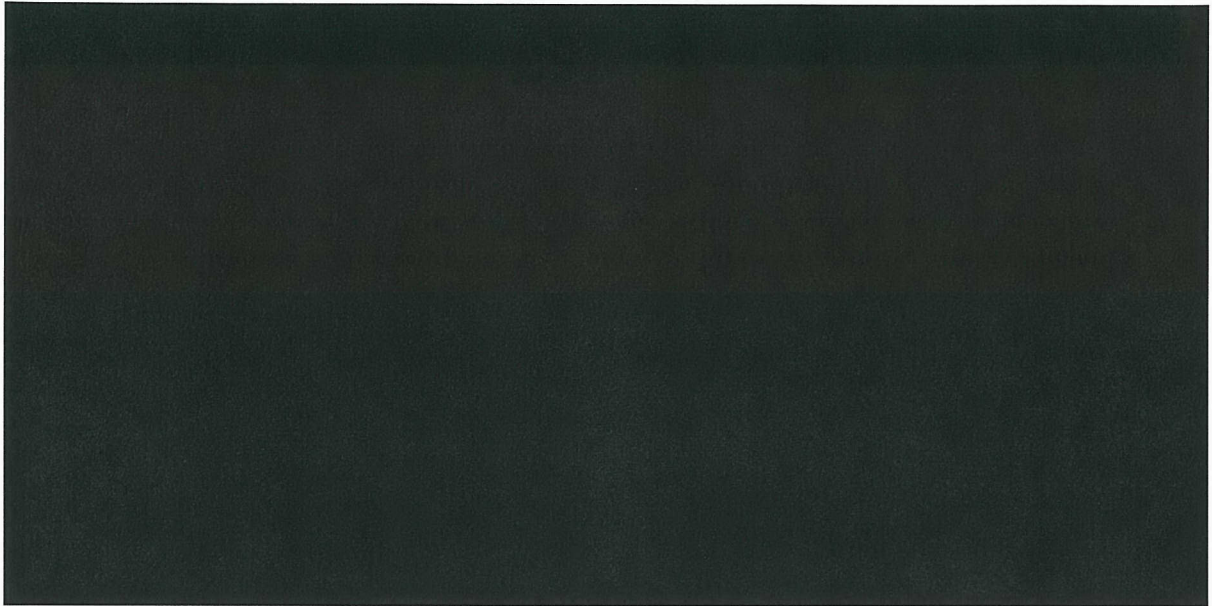
**Table 3**








The chart demonstrates the clear and significant benefits of the SOTW promotions by showing the marked degree to which purchases of songs featured in a SOTW promotion increase following the week during which the song is available, compared to the week prior to the applicable SOTW promotion. More complete information on the SOTW is attached at Exhibit C. While other factors may contribute to the increase in sales, the significant impact of the SOTW is undeniable. The songs generally experience a many-fold increase in iTS sales after being featured as a SOTW. Most importantly, this benefit is felt by all participants in the value chain, from iTS to the record label to the composer of the selected song.

**Table 4**A large black rectangular box redacting the content of Table 4.

25. And these numbers do not take into account the multiplier effect alluded to earlier, in which awareness of an artist or song due to exposure on iTunes translates into greater sales for that artist or song from other online distributors and physical CD retailers. We have observed that an artist's song being featured as SOTW can create a springboard effect for success industry-wide.

**Table 5**A large black rectangular box redacting the content of Table 5.

As shown above, the tracks "Bad Day" (by Daniel Powter) and "Over My Head" (by The Fray) both enjoyed significant increases in sales on iTS following their being featured as a SOTW. However, the benefits to these tracks (and thus to the relevant copyright owners) of being selected and featured by iTunes as a SOTW go beyond increased sales

on iTunes. For example, the track “Bad Day” was the SOTW during the week of August 2, 2005. On October 8, 2005, the track debuted on Billboard’s Adult Top 40 chart at #38. By April 8, 2006, the song was #1 on the Adult Top 40 chart and #1 on Hot 100 chart. The track “Over My Head” was the SOTW during October 11, 2005 and debuted on Billboard’s Adult Top 40 on November 19 at #37, peaking on March 25, 2006 at #5 and on the Hot 100 in June at #8. Neither artist was on these charts at the time of their being featured as our SOTW, and they each rose quickly up the charts following their success on iTunes. It is my opinion, based on my experience in the music business, that each song’s climb up the charts was directly influenced by its being featured as our SOTW. Along with other promotional efforts by the artists and their labels, my experience leads me to believe that iTunes’ selection of these tracks as SOTWs, and the increased exposure within iTunes resulting from that selection, helped propel these new artists toward the top of the overall Billboard charts.

26. The SOTW and other iTunes promotions, coupled with the user-friendly interface of the storefront and the ready availability of track samples, album reviews, background information about artists, and links to other songs and bands that mesh with users interests all reflect the core purpose of iTunes -- which is to increase public exposure to, and purchase of, more music. iTunes enables the public to discover more new music, learn about new artists that they might otherwise never hear, explore different genres that they might previously have overlooked and track down long-forgotten (and often out-of-print) songs. What we offer is an opportunity that is not readily available in the physical world: in effect, we lower transaction costs and barriers for consumers by making it easier for them to hone in on music and artists they are interested in, and to gain



awareness of new bands and tracks that they might not otherwise come across, let alone purchase. The result is to increase overall levels of music consumption by facilitating music purchases that likely would not take place in the physical world.

27. For these reasons, iTunes has been called the “archetypal Long Tail company,” (*New York Times Magazine*, Sept. 10, 2006) and credited with expanding the breadth and diversity of musical works to which consumers are exposed and ultimately purchase -- thereby enabling publishers and music companies to “exploit niche demand more effectively than ever before . . . .” Musical works that are unable to obtain meaningful shelf space at physical retail outlets are as readily accessible to iTunes customers as the hit records that dominate the aisles at CD stores.

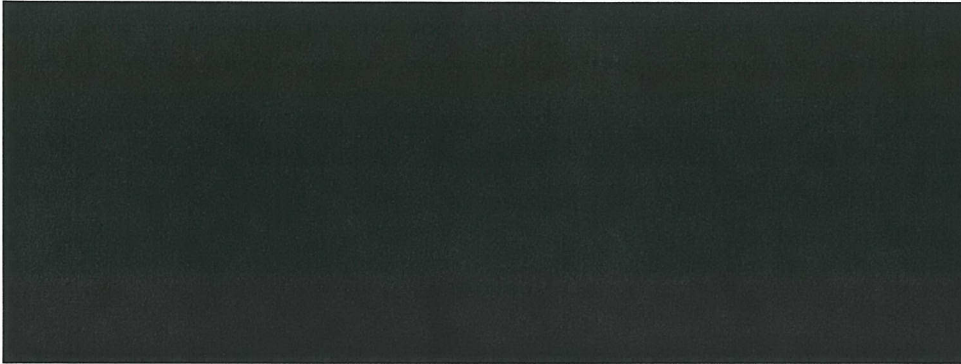
28. Universal Music recently launched an initiative in which it made approximately 3,000 songs from its out-of-print catalog of European artists available for re-release online. In just nine months, online consumers purchased more than 250,000 tracks from this out-of-print catalog, which featured some songs that had been unavailable for over three decades. In noting the initial success of the initiative, Universal stated:

Overall, these results lend weight to author Chris Anderson’s Long Tail theory . . . that given the growing choice and diversity of music that is legitimately available through the Internet consumers will be increasingly drawn to recordings beyond current hits. In this scenario, the total sales of this repertoire (the long tail) can match or exceed those of the hits. (Universal Press Release, October 17, 2006).

At iTS, the percentage of sales attributable to the relatively narrow band of hit songs and hit records is significantly lower than the comparable metric for physical CD outlets such

as Tower and Wal-Mart, highlighting the ability of iTS to drive sales of a broader and more diverse array of musical works. This is represented in the following table:

**Table 6**



Based on my experience in the music business, I understand that the significant extent of our sales of music beyond the Top 200 hits is not typical of traditional retail environments, and is a unique benefit offered to consumers and copyright owners by digital distribution.

29. Independent record labels have enjoyed a boost in business in recent years, thanks in part to the degree to which iTunes and other digital music outlets broaden consumer awareness of, and exposure to, artists and albums that lack the marketing muscle provided by major labels and large retail CD outlets. As the graphic below shows, we continually highlight indie content in iTS on our various Indie Spotlight pages.



There is also evidence showing that iTunes and other digital distribution outlets for music are spurring the record labels to expand the number of albums they release each year, due to the lower costs associated with manufacturing, transporting, and inventorying digital releases. Earlier this year, *Billboard* [March 18, 2006] reported that the number of albums released last year was a record-breaking 60,331, a 35.6% increase over 2004's total of 44,476, which itself was 16% higher than the 2003 total. *Billboard* stated that "[l]ast year's increase in releases is driven by an influx of digital-only, indy-released product." SoundScan defines a digital-only release as those albums in which 99% or more of sales occur through digital services. Thus, iTunes and other online retailers are



helping to drive the release of more music by record labels, thereby enhancing the ability of composers and publishers to find an audience for their works.

30. iTunes is expanding the music marketplace for all industry stakeholders, including copyright holders, and not just cannibalizing sales from physical outlets. This process of enlarging the overall pie by lowering pre-existing barriers to transactions requires continued investment and innovation in order to maintain an interface with customers that facilitates transactions and incremental sales increases. These investments are aimed not just at acquiring incremental customers, but at turning those customers into habitual purchasers of music online. iTunes has gained traction as a reliable, customer-friendly and secure outlet for digital music transactions, and has thereby played a substantial role in transforming the online realm from a hostile environment for copyright holders into a secure distribution channel that provides artists and publishers with a significant new revenue stream.

#### **IV. THE MARKETPLACE IN WHICH WE OPERATE IS HIGHLY COMPETITIVE, RAPIDLY EVOLVING, AND CONTINUALLY POSING NEW CHALLENGES**

31. While iTunes has met with noteworthy success since launching our store in the United States in 2003, there have been competitive challenges every step of the way. I believe a key reason for the market's acceptance of our offering has been the selection of a price point for our product that is attractive to consumers, thereby encouraging use of the store and allowing us to be competitive with the two sectors of the market against which we compete, while still covering our operating costs and permitting a small margin for profit.

32. Not only must iTunes compete with other online music services for market share in providing legal online music, but we face powerful competitive pressure from online music piracy and the physical retail world. It is worth looking at each of these in turn, to see how they have affected (and continue to have an impact on) our business model and offering and our pricing structure.

33. Although we compete with a broad range of entertainment and music products and services, illegal music -- including peer-to-peer ("P2P") services -- is our most formidable competitive rival. The emergence of P2P services was facilitated by significant advances in terms of technology and better access to the Internet of the late 1990s. More and more households began to use the Internet regularly for email and free access to information and content generally, and the growing speeds and falling prices of broadband access meant that it became more viable to distribute large media files over the internet by email or by using increasingly sophisticated filesharing networks. I am informed and believe that P2P networks sprang up on a worldwide basis and spread quickly, with services such as the old Napster, KaZaA, Grokster, and Gnutella (to name only a handful) allowing individuals to find and distribute music and video (the vast majority of it without authorization from rights holders) quickly, easily, anonymously and, most importantly, for free. The combination of pervasive broadband networks, increases in storage capacity, and more efficient file compression technologies all combined to spur the emergence of services and technologies predicated upon facilitating online music piracy.

34. Although the recording industry has taken legal steps to combat these networks in the U.S., with some notable court victories, its overall success in combating piracy through legal action has been limited. Each successful yet costly lawsuit can be matched by the arrival of dozens of new networks and the many millions of individuals around the globe that continue this illicit practice. The demand for free digital music has simply grown and the technology for distributing it illegally (together with the quality of the media being distributed) has improved.

35. In light of the perceived limited reach and impact of the legal action taken against piracy, we believed that the best way to successfully compete with the online pirates would be for us to offer a compelling consumer alternative to illicit downloading. Obviously we will never be cheaper than free, but we always hoped that if we were to offer a better product at a fair and competitive price, we would be able to attract to our service those individuals who would otherwise turn to illegal download services to obtain their music.

36. To this end, we had to come up with a product that was attractive in terms of both substance and pricing. One method to achieve this was by the manner of distribution of content. As I have described above, we designed a music store interface that is extremely easy to use yet highly sophisticated in terms of its functionality, and combined it with strong brand recognition to reassure people of the quality of the product. iTunes seamlessly blends into the iTunes Jukebox software so that the task of buying songs, adding them to a user's personal collection and then transferring them onto



a CD or a compatible portable digital media player is not only an enjoyable retail experience but also as technologically painless as possible.

37. Another method we employed was carefully selecting the correct compression and DRM technology to sell our songs. We chose the AAC codec to encode our music as it provides near CD quality sound at higher compression rates than the MP3 files more commonly favored by illegal file sharers. This means that the files purchased from iTS are smaller than those being distributed via peer-to-peer networks, which results in quicker download times, greater ease, and better quality music in a product that also takes up less space on an individual's computer hard drive, portable player, or mobile phone. Furthermore, we developed and employed our own proprietary DRM, Fairplay, in conjunction with the AAC file format, in order to ensure that there was a fair balance between the ability of the user to enjoy the music and proper protection of the rights of the copyright holders. iTunes has played a significant role in helping to enhance the security and revenue opportunities afforded composers in the online world.

38. As I stated above, piracy has been a key factor in determining our price point in the U.S. and other markets around the world. It may be stating the obvious, but as we are competing with a product that is free, we need to pick a price that balances that reality against the quality of our product and our variable costs for distributing that product, which affords iTS the opportunity to earn a profit. We believe that a large measure of our success is attributable to the fact that we price songs for less than a dollar, a price point that diminishes the financial "rewards" of pirating "free" music. And we believe that if the price of our songs were to increase, many people would switch back to

piracy. From my perspective and experience, the \$0.99 per-track retail price represents the price point that maximizes overall revenues from iTS for all industry stake-holders. If we had to raise that price, I believe total sales transactions and aggregate revenues would fall precipitously.

39. The other principal competitor we face is, of course, the retail market for CDs. We have always viewed our product as going head to head with CDs, and in fact, as noted earlier, a significant portion of our sales consist of sales of entire albums, as opposed to individual tracks. Although digital downloads and CDs do have differing characteristics in terms of functionality, and each has certain advantages over the other, both provide the consumer with essentially the same thing: a permanent copy of his or her chosen song, album or music video, which can ultimately be played back at will through a compatible computer, portable digital music player, and even a CD player or stereo. Accordingly, one of the factors we have to take into account when setting our price point is the retail price of physical CD albums and single. We have found that consumers generally expect that digital albums should cost somewhat less than their physical counterparts. Given that, unlike CDs, we provide no tangible item to the consumer, and our digital products are wrapped in DRM unlike their CD counterparts, these consumer expectations would not appear to be unreasonable. In any event, as we need to deal with the market reality of these consumer expectations, our albums tend to be priced somewhat lower than physical CDs.

40. When viewed in light of fierce competition from online retailers and music store chains, the relative infancy of the retail market for online music and the

erosion of the music market generally through piracy, [REDACTED]

[REDACTED]

[REDACTED]. In essence, [REDACTED]

[REDACTED], and we believe that our relative success in the marketplace bears some testament to the correctness of this approach.

**V. DEVELOPING THE iTUNES STORE COST TENS OF MILLIONS OF DOLLARS AND REQUIRES MILLIONS OF DOLLARS OF ONGOING INVESTMENT AND EXPENSES**

41. Digital distribution of music to retail consumers is neither simple nor cheap. iTunes has committed a substantial amount of capital and resources into creating a storefront and distribution network that is customer-friendly, reliable, and secure. A substantial number of users with accounts may not be regular or repeat customers -- and our business model is not predicated upon recurring revenue streams -- so there is an ongoing need for investment and innovation aimed at rekindling interest from prior customers and recruiting new ones. [REDACTED]

[REDACTED]

[REDACTED] To continually attract repeat buyers and increase the frequency of other buyers, we are constantly investing in making the store easier to use and more appealing to consumers.

42. Our operating margin is saddled with substantial costs, reflecting both the investment required to develop and bring the iTS to market and the expenses associated with ongoing maintenance and operation. It is true that online music does not face the



same type of manufacturing and distribution costs that the physical retail model faces in manufacturing and physically distributing a CD. However, online music involves a whole host of other very significant costs that do not have any counterpart in the offline world.

43. iTunes has invested [REDACTED] into developing a store that provides music shoppers with a comprehensive catalog and an interface that is fast, clean, intuitive, and easy for even beginners to use. The sophisticated yet user friendly software applications, together with the encoding and digital rights management techniques that form an integral part of our strategy to provide an attractive and competitive alternative to piracy, have been extremely costly to develop and to maintain. iTunes has invested substantial capital in the development and implementation of its hardware and software for iTS, including its “back office” and financial services infrastructure, as well as its online store interface, and in procuring and maintaining sufficient bandwidth to be able to deliver a high-quality service during peak hours with no discernible contention issues. A substantial portion of the millions in development costs incurred by iTunes is related to the engineering costs associated with designing and deploying the software codes and hardware devices necessary to ensure that the store functions in a secure, reliable and customer-friendly manner, and can adapt readily new features and capabilities needed to keep pace with, and ahead of, a highly competitive marketplace.

44. These costs continue on an ongoing basis, as illustrated by the P&L statement attached at Exhibit D. The most significant cost that iTS has to meet is that of

the licensing agreements that it has entered into with record labels to provide its extensive catalog of music. Royalty payments to record labels, including payments by the labels for publishing rights, [REDACTED] [REDACTED]. Much as in the physical retail market, the bulk of these royalty payments go to the record labels for the sound recording right, (from which portion artists are paid their royalties), but the right to copy and distribute the musical composition also is included in this amount. Again, as in the physical retail market, the record labels bear responsibility for distributing a portion of the royalties paid to them by iTunes to songwriters, in accordance with their agreements with the publisher and composer agencies. iTunes' costs would rise significantly if, following the conclusion of this proceeding or at some other time in the future, the record companies stopped sublicensing mechanical rights from copyright holders or if the sums record companies must pay to publishers for mechanical rights were to increase (i.e., any such increase undoubtedly would be passed through to iTunes).

45. As shown by Exhibit D, bandwidth costs are a significant component of our variable costs, [REDACTED]. As the service grows, our bandwidth needs to increase as well, so we must continue to invest in the development and maintenance of our product distribution infrastructure.

46. Our distribution infrastructure not only must be fast and reliable, but it also must be secure in order for iTunes to stay one step ahead of the online pirates. Since its launch, both iTunes and the iTunes Jukebox have been through numerous systems upgrades or versions not only in order to improve the experience for the end user but also to

maintain the effectiveness of the Fairplay DRM, which has been (and continues to be) the subject of hacking attempts. We have needed to stay one step ahead of projects that seek to break the DRM and thereby place the rights of the publishers and the labels at risk. Our continued investments are protecting the rights holders' interests, but at a significant cost to iTunes. There are also risks and costs associated with the uncertain and still-evolving legal framework governing online music distribution. For instance, performing rights organizations have taken the position that their right to a performance royalty is implicated in connection with the manner in which permanent song downloads are offered and distributed online. While we do not share this view (and it certainly does not prevail in connection with the offering and distribution of music at physical retail outlets), it represents an ongoing issue.

47. Another key cost is that of marketing. There is a real need to educate the public on the benefits of purchasing legal online music, particularly given the incumbency of the physical retail market (and the familiarity of the music buying public with CDs), the infancy of the legal online music market, and the fairly established nature of illegal downloads. The fact that we don't have walk-in stores like physical retailers do is a disadvantage as well as an advantage: although we do not have to bear the same types of overhead costs as a walk-in store, we don't get foot traffic in the way that physical stores do, and so have to rely upon people visiting Apple's website or downloading the iTunes Jukebox software. This requires constant reaffirmation of the benefits of our service through specific marketing initiatives that let consumers know about iTunes, where to locate it, how to use it, and offering enticements for them to do so. This is a major expense to us each year, [REDACTED]



██████████. iTS also makes gift cards available to the public through a variety of retail outlets and promotional initiatives. While these cards help to expand our customer base by driving consumers to the store who might otherwise not visit, the costs of making and distributing the cards -- and partnering with retail outlets or undertaking card-related promotions -- effectively reduce the margin on tracks purchased with them. We view the costs associated with gift cards as a marketing expense.

48. Consumer awareness of our product also has developed via advertising campaigns that feature iTunes and iPods. Such advertising is important to developing and expanding consumer interest in our digital music offerings, and has helped to strengthen the public awareness of digital distribution as a new and effective mechanism for purchasing music. [REDACTED]

[REDACTED] This cost element is not reflected in the attached P&L. Of course, the benefits to iTS and all participants in the music industry from Apple's overall music advertising are not limited just to iTS' proportional share.

49. Credit card processing fees associated with iTS are another key ongoing cost that must be taken into account when considering the cost structure of our permanent download business. These fees are growing rapidly each year, [REDACTED]. [REDACTED]. The size of these fees as a percentage of retail revenue can vary from quarter to quarter, due to the fact that there are certain minimum fees per transaction payable to the credit card companies, and depending upon the number and type of music products (songs or albums) purchased by iTS customers.

In particular, the sale of single downloads generates proportionally far higher credit card transaction costs. As a result, our margins on small purchases typically are either non-existent or negative. In fact, we can only survive if we are generally able to convince customers to purchase multiple tracks at a time. Moreover, because the vast majority of customer transactions are consummated with credit cards, we face a significant amount of credit card fraud risk (copyright owners demand payment for downloads even if we do not get paid due to fraud). The fraud risk is heightened in the permanent download business -- as compared to physical retailers and other online business models -- because,

[REDACTED]

Moreover, due to heightened public concern over online fraud and identity theft, we also incur higher fraud prevention costs than our competitors at physical outlets. In short, in any quarter, credit card fees constitute a significant drag on our margins.

50. The margin figures shown in Exhibit D [REDACTED]

[REDACTED]

51. The fact is that, even though we are optimistic about the future of the online music marketplace and heartened by iTunes' success so far, there are significant

risks posed by very high operating costs, the infancy of the market, the evolving nature of business models attempting to provide digital music to customers, and the competitive pressures that we face -- in particular from piracy. This is a business of very small margins, but margins nonetheless. It is precisely because iTunes recognizes this that, although faced with an extremely competitive marketplace, iTunes has never lost money on a global basis.

**VI. A FAIR ROYALTY RATE WOULD ENSURE THE CONTINUED PRESERVATION AND EVOLUTION OF LAWFUL DISTRIBUTION OUTLETS FOR DIGITAL MUSIC DOWNLOADS**

52. Any reasonable royalty should reflect the substantial investments and risks we have incurred to date, the competition and limited margins that iTS faces, and the significant value we provide to copyright holders. An excessive royalty rate would stifle any effective competition with piracy or the physical retailers, as we would either be forced to raise prices, limit further investment in present and future services or even simply drop out of the market. The net result would be the same: the adoption of legal digital music would slow significantly or fall, and this would naturally have ramifications for everyone in the industry, including the artists and composers.

53. As I understand it, a rate must be set in this proceeding on the basis of various statutory factors involving different objectives. As this marketplace begins to evolve from the stage of early adoption, consumers will be faced with a choice of where to obtain new music going forward. The threat of piracy is real and shows no signs of diminishing in the next five years. To encourage continued consumer migration to lawful digital distribution platforms, and to encourage companies like Apple to continue to incur



the risks and investments incurred by iTunes to build legitimate outlets for the digital distribution and consumption of music, the online music industry should not be saddled with excessive costs. To the contrary, to make the tremendous investments necessary to create and grow this market more reasonable, the costs associated with our business need to be reduced.

54. Apple has been successful to date furthering the availability of creative works to the public. However, given the prevalence and easy accessibility of free illegal music, raising our costs directly (or indirectly by raising costs on the record labels that supply us with content) could result in reducing our presence in the marketplace. Importantly, the rate for digital downloads should not be set higher than the rate for physical CDs. To the contrary, the rate should be lower than the rate for physical CDs because digital retailers such as iTunes have had to incur such substantial risks and development costs simply to establish a lawful digital distribution platform. In addition to the costs associated with establishing and growing a new distribution channel, ITS and other digital retailers are continuing to make new investments that are expanding both the customer base and the base of musical compositions involved in DPD transactions. These factors, in addition to others mentioned earlier in my testimony, all militate in favor of setting a royalty rate for DPDs that is lower than the rate for physical CDs.

55. On September 28, 2006, Apple entered into an agreement settling copyright royalty litigation in the United Kingdom. The settlement and license are attached at Exhibit E. As a result, [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] in the musical compositions sold on iTunes. Certain issues [REDACTED] revenue remain to be litigated by the parties. We believe the settlement represents a fair compromise to settle litigation in that marketplace. It is not, however, directly analogous to the current proceeding, given the different market conditions and precedents, different legal rights involved in the UK and covered by the license, and the different legal standards that I am told apply there. At most, it provides an indication of a ceiling on a reasonable rate (provided the UK Tribunal ultimately sets a reasonable revenue definition).

56. Any increase in the royalty rates we pay for musical works would have a significant adverse impact on the commercial viability of iTunes. We have ensured that, notwithstanding the very real pressures and difficulties this business faces, iTunes on a global level has always made a profit or broken even, with the hope of building on that base for everyone's benefit. However, this is a risky business, with small margins that can ill-afford to be freighted with additional costs. As noted above, this industry needs reduced, not increased, costs in order to continue to attract the investments necessary to its growth and stability.

## VII. CONCLUSION

57. I have been informed that DiMA's expert witness, Margaret Guerin-Calvert, believes a mechanical royalty rate in the lower end of a range of 4-6% would be appropriate. In light of my experience with the iTunes business worldwide for the past

several years, I believe her recommendation is both reasonable and appropriate. As a result, I support DiMA's proposed rate of 4.1% for permanent downloads.



I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief:

Eddy Cue  
Eddy Cue

11/28/06  
Date

A

B



**This exhibit contains restricted information that is  
subject to a confidentiality agreement and has  
been redacted from the publicly filed version**

C

**This exhibit contains restricted information that is  
subject to a confidentiality agreement and has  
been redacted from the publicly filed version**



D

**This exhibit contains restricted information that is  
subject to a confidentiality agreement and has  
been redacted from the publicly filed version**

E



**This exhibit contains restricted information that is  
subject to a confidentiality agreement and has  
been redacted from the publicly filed version**